DEPARTMENT OF STATE REVENUE

01-20140687.LOF

Letter of Findings: 01-20140687
Individual Income Tax
For the Years 2010 and 2011

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

Indiana individual failed to report income received as the sole shareholder of an S Corporation, failed to show that the income tax assessment overstated her shareholder income, and owed tax on that income.

ISSUE

I. Individual Income Tax - Audit Assessment.

Authority: IC § 6-8.1-5-1(c); Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579 (Ind. 2014); Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); 45 IAC 3.1-1-66.

Taxpayer argues that an audit assessment of individual income tax was incorrect.

STATEMENT OF FACTS

Taxpayer is an Indiana resident and sole shareholder of a fast-food restaurant organized as an S Corporation. The Indiana Department of Revenue ("Department") conducted an audit of Taxpayer's restaurant business and Taxpayer's own individual income tax returns. The audit resulted in an assessment of additional income tax. Taxpayer disagreed with the assessment and submitted a protest to that effect.

I. Individual Income Tax - Audit Assessment.

DISCUSSION

Taxpayer maintains that the assessment of additional income tax overstates the amount of tax actually due.

As a threshold issue, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." Indiana Dep't of State Revenue v. Rent-A-Center East, Inc., 963 N.E.2d 463, 466 (Ind. 2012); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007). Consequently, a taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Further, "when [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] defer to an agency's reasonable interpretation of [the] statute even over an equally reasonable interpretation by another party.'" Dept. of State Revenue v. Caterpillar, Inc., 15 N.E.3d 579, 583 (Ind. 2014). Thus, all interpretations of Indiana tax law contained within this decision, as well as the preceding audit, are entitled to deference.

A. Audit Results.

The Department's audit found that Taxpayer "presented very minimal records and documents of her [restaurant] business history." A review of the available records found that Taxpayer had 2010 and 2011 income from three sources. Taxpayer received distributive income from her restaurant which was organized as an S-Corp. Taxpayer received salary and wages from the restaurant business. Taxpayer received interest income.

Taxpayer failed to report her income for 2010 and 2011. In calculating the amount of tax due, the audit "allowed

the $1,000 personal exemption and the credits for state and [county] withholding taxes paid.

The Department had previously audited Taxpayer's restaurant business. The audit of the S-Corp. found as follows:

> The examination disclosed that the [restaurant] understated the gross sales reported on its ST-103s. No explanation could be given by the [restaurant] on this difference. A percentage of this understatement was determined and was applied to the sales of the current audit periods as reported by the [restaurant] on its ST-103.

B. Taxpayer's Response.

Taxpayer previously challenged the restaurant audit. A separate Letter of Findings ("LOF") addresses that protest and found that Taxpayer failed to establish the audit findings were incorrect. The LOF concluded as follows:

> Taxpayer failed to maintain records necessary to verify its sales tax liability, illegally diverted sales tax it collected and held in trust for the state, and failed to establish that the audit assessment overstated its tax liability.

C. Hearing Analysis.

This Letter of Findings addresses Taxpayer's protest challenging the income tax assessment.

An S Corporation, such as Taxpayer's restaurant, normally does not pay income tax. 45 IAC 3.1-1-66, states that, "Corporations electing Subchapter S status under Internal Revenue Code § 1372 . . . are exempt from adjusted gross and supplemental net income tax on all income except capital gains . . . ." Rather than taxing the income at the business level, the S Corporation's income is passed through to the shareholders. The shareholders then must report the income on their own income tax return. 45 IAC 3.1-1-66 further states that, "Subchapter S corporation shareholders are taxed on their distributive shares of income at the individual income tax rate."

Other than simply disagreeing with the assessment and citing difficulties in paying that amount, Taxpayer has provided no substantive information refuting the audit's conclusions. The companion audit of Taxpayer's restaurant business established that Taxpayer underreported the restaurant's sales. Those additional sales "flowed through" to Taxpayer as the restaurant's sole shareholder. Taxpayer failed to report that income and - regardless of the difficulties she had in operating her business - now owes income tax on that amount.

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FINDING

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Taxpayer's protest is respectfully denied.

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